

November 30, 2001

Todd Younkin, Associate Fiscal Analyst
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Room 110 Capitol Building
Helena MT 59620-1711

Dear Mr. Younkin:

The following responses are offered to your questions of November 20, 2001.

1 Question: 17-6-305, MCA requires the Board of Investments to “include a report on the investments made under [17-6-305] as a part of the information required by 17-7-111.” Please provide the latest copy of this report.

1 Answer: The Board’s Fiscal Year 2000 Annual Report is enclosed. The Fiscal Year 2001 Annual Report is nearly complete.

2 Question: Prior to July 1, 1999, 90-3-203, MCA required the Board of Investments to “submit to the Governor by January 1 of each odd-numbered year, or when otherwise requested by the Governor, a report describing the [Montana Board of Science and Technology Development] programs and accomplishments.” What reports and/or status updates, providing similar information, are currently presented to the Governor and/or Legislature detailing the status and related results of MSTA-related loans?

2 Answer: Section 90-3-203, MCA was repealed on July 1, 1999, when the Board of Investments was made successor in interest to the former MSTA portfolio. The Board manages the portfolio under its governing laws and does not prepare a specific report on the status of the MSTA portfolio as was required under the repealed law. The Board does respond to legislative requests for information on the status of the portfolio.

3 Question: What are the Board of Investments procedures for identifying and closing out loans in the following categories:

- a) Negotiated as “paid” before the full amount is received (in good standing)?
- b) Identified as “uncollectable” or in default (written off)?

3 Answer: A “negotiated” settlement of outstanding principal may occur if we believe the borrower’s business is likely to fail in the absence of such settlement. Because a failure of the business could result in the loss of all outstanding principal, a settlement may occur to reduce the potential loss to the Coal Tax Trust.

A non-collectable debt, such as an outstanding loan to a company in bankruptcy, would be written off when there is no longer a reasonable chance of collecting any of the outstanding principal balance.

4 Question: In each case, what or who provides the authority (statutory, administrative, or other) to do so?

4 Answer: Board staff would negotiate any debt settlement on outstanding principal pursuant to general direction of the Board. The settlement’s purpose would be to “minimize the risk of loss” as required under the prudent expert principle governing the Board’s management of public funds.

Once a debt is determined to be “non-collectable” it would be written off as required by Generally Accepted Accounting Practices. In both instances, the proper entries would be made on the state accounting system so loss of Coal Tax Trust Principal could be identified.

5 Question: What is the fiscal status of and future outlook for the overall program, to include:
a) What is the return on investment for all loans made by the Montana Board of Science and Technology Development since its inception?

5 a) Answer: It is not possible to calculate return on investment of the MSTTA portfolio because of the different types of loans made and the types of agreements used to structure the loans.

?? University System research and development loans are structured to pay back \$300,000 annually, all of which is currently applied to principal. Given the size of the annual payment relative to the \$8.5 million in outstanding principal, we assume there will be no investment return on these loans and that it will require many years just to repay principal.

?? Private facility research and development loans did not have computed interest rates. The loan agreements required that the borrower repay 2 ½ times the principal. Investment return on these loans will depend upon the time taken to repay the entire amount. (A shorter pay back period increases the return, while a longer pay back period decreases the return.)

?? Most seed capital loans are structured as five to ten year debentures with balloon payments due upon debenture maturity. Interest, either simple or compounded interest, is due, along with the total principal, when the loans mature. Due to the uncertainty of collecting the interest at the end of the loan term the Board does not accrue interest on these investments. In the absence of interest accruals, there is no investment return. If and when the loans are paid in full, including principal and interest, the return on individual investments can be calculated.

5 b) Question: What is the overall amount of funds loaned and pay backs received to date for each separate source of funding?

5 b) Answer: The loans funded and the pay back received through October 1, 2001 are shown on the next page.

<u>Company Name</u>	<u>Type of Business</u>	<u>Date Funded</u>	<u>Loan Amount</u>	<u>Principal Paid (1)</u>	<u>Interest Paid (1)</u>
Chromato Chem, Inc.	HPAC biotechnology products	12/01/89	\$350,000	\$1,650	\$1,850
Gateway Software	Computer Software for IBM	01/01/90	509,150	334,150	296,000
Nurture, Inc.	Oat-based Additive	08/01/89	1,225,000	719,786	11,563
Lattice Materials	Infrared Laser Optics	01/01/90	555,000	555,000	448,426
Mycotech, Inc.	Fungi Related Bio Products	04/01/91	1,211,013	350,000	837,635
Optima Industries	PCB Drilling System	07/01/91	700,000	139,500	160,500
Ultrafem, Inc.	Menstrual Collection Device	11/01/91	700,000	209,698	
TMA Tech/Schmitt Industry	Detecting Instruments	10/01/91	1,455,956	158,921	31,623
Northern Rockies Venture	Venture Capital Company	09/01/93	1,000,000		32,200
Glacier Venture Fund, L.P.	Venture Capital Company	04/01/95	1,000,000		
Positive Systems	Computerized Aerial Photos	02/01/94	550,000		
Keep It Simple Systems, Inc.	Computer Solar Panels	04/01/96	75,000	16,072	
Pasta Montana	Dry Pasta Products	07/01/96	350,000	337,449	102,514
Safe Shop Tools	Brake Drum & Wheeling Hubs	02/01/97	162,500		
Spectrum Pool Products	Swimming Pool Products	09/01/95	400,000	400,000	64,161
Yellowstone Ace Hardware	Specialized Home Improvements	10/01/95	100,000	100,000	18,922
Pasta Montana	Dry Pasta Products	07/01/96	500,000	480,198	167,552
Deaconess Research Institute	Billings	05/29/92	500,000	205,131	200,789
McLaughlin Research Institute	Great Falls	11/17/93	500,000	72,168	53,570
University Systems		07/91	9,727,506	1,250,246	954,754
Total			<u>\$ 21,571,125</u>	<u>\$5,329,969</u>	<u>\$3,382,059</u>

(1) Through October 2001

5 c) Question: What is the current status of loan repayments as they are received by the Board of Investments? Specifically, how much, if any, is used to pay Board of Investments administrative costs; and how much, if any, is deposited to the Coal Severance Tax Permanent Fund.

5 c) Answer: Administrative costs for managing the MSTA portfolio consists of a .25 FTE, other staff time when required, and occasional contracted legal costs. Normal costs should range from \$20,00 to \$30,00 per year, unless our collection efforts require extensive legal assistance. All administrative costs for managing the MSTA portfolio are paid utilizing the same cost allocation system the Board uses to pay the costs of managing its entire portfolio. The Board allocates its costs among; 1) investment pools; 2) fixed income investments; 3) private equity investments; and 4) loans/mortgages. The MSTA portfolio is included in the "loans/mortgages" category, along with the other in-state investments managed by the board.

Pursuant to the enclosed Attorney General's Opinion, any income currently earned on the MSTA portfolio is deposited in a state special revenue account until sufficient funds are available to complete the \$2.0 million in grants to the University System authorized by the 1997 Legislature. A balance of \$441,910 remains to fully fund these grants.

5 d) Question: What are the Board of Investments projections for overall impact on the Coal Severance Tax Permanent Fund and other state funds upon conclusion of all loan agreements entered into by the Montana Board of Science and Technology?

5 d) Answer: While there will be loss of Coal Tax Trust principal, the actual loss amount cannot be determined at this time. We will continue to protect trust principal as best we can, but if MSTTA-funded businesses fail despite our efforts, there will be insufficient loan collateral available to recover principal.

During the term of these loans any interest income in excess of that required to fund the remainder of the \$2.0 million University grants will be deposited in the Permanent Fund Income Account and ultimately transferred to the State General Fund.

5 e) Question: What is the projected date for the conclusion of those loan agreements?

5 e) Answer: The latest maturing debenture is due in April 2006. Any structured settlements of these debentures may extend well beyond that date.

Those loans with some type of formal amortization schedule should mature by 2023.

The Research and Development loans to the University System under the current pay back schedule of \$300,000 annually will not be fully paid until approximately 2029. This date assumes that all payments are applied to principal until the principal is paid in full.

5 f) Question: For all loans made since the creation of the Board of Science and Technology Development, excluding the information in question d) above, what is the overall economic impact to the State of Montana and/or the programs involved, to include jobs created, jobs maintained, patents obtained, and any direct or indirect effects on per capita income and revenues to the people of Montana?

5 f) Answer: The last report issued by the Board of Science and Technology Development was dated December 20, 1996. That report listed the economic benefits as shown below:

<u>Loan Type</u>	<u>Jobs Created</u>	<u>Wages Paid</u>	<u>Income Taxes</u>	<u>Property Taxes</u>	<u>Leveraged Funds</u>
Seed Capital	245	\$26 Million	\$1.6 Million	\$218,000	\$139.0 Million
Job Investment	30	\$752,000	\$25,000	\$3,700	\$10.4 Million
R & D	247				\$115.4 Million

6 Question: What is the current status of the venture capital companies approved by the Montana Board of Science and Technology Development? For each venture capital company, please identify the portion of the portfolio attributed to Montana-based and Montana-related investments, and specifics on each of those identified investments, to include jobs created or maintained and direct or indirect benefits to the people of Montana.

6 Answer: The MSTA funded two venture capital companies, the Northern Rockies Venture Fund and the Glacier Venture Fund. The Northern Rockies Venture Fund is fully invested, while the Glacier Venture Fund is not. The individual investment made by these companies are listed below:

NORTHERN ROCKIES VENTURE FUND

<u>Company</u>	<u>Business Type</u>	<u>Investment</u>	<u>Current Est. Value*</u>	<u>Principal Location</u>
H.S. Trask, Inc.	Rugged footwear	\$ 200,000	\$ 200,000	Bozeman
Glacier Venture Fund	Venture Capital Fund	25,000	25,000	Helena/Polson
Safe Shop Tools, Inc.	Heavy-duty tools	162,600	60,000	Missoula
Sterile-Safe Systems, Inc.	Anti-bacterial agents	93,627	0	Bozeman/Helena
Nutritional Labs. International	Vitamins/herbs	122,708	2,489,494	Lolo
Big Sky Transportation, Inc.	Rural airline	200,000	128,000	Billings
Jore Corporation	Power tool accessories	115,000	0	Ronan
Ligo Cyte Pharmaceuticals	Drug/treatment products	180,000	180,000	Bozeman
Lynay Healthcare, Inc.	Health care	278,500	1,014,770	Cibolo, TX
Environmental News Network	Internet environmental news	75,000	100,000	Sun Valley, ID
Iron Clad Performance Ware	Protective clothing	<u>180,000</u>	<u>823,559</u>	Santa Monica, CA
TOTAL		<u>\$ 1,632,435</u>	<u>\$5,020,823</u>	

GLACIER VENTURE FUND

Ligo Cyte Pharmaceuticals	Drug/treatment products	\$ 369,103	\$ 369,103	Bozeman
Imple Max Equipment	Tractor attachments	<u>375,000</u>	<u>375,000</u>	Bozeman
TOTAL		<u>\$ 744,103</u>	<u>\$ 744,103</u>	

Both funds have \$1,000,000 in MSTA funds

Glacier is not fully invested. 100% of its investments are in Montana companies.

Northern Rockies Venture Fund is fully invested with 67% invested in Montana based companies.

*Estimated Value based on estimates provided by the venture fund companies.

Sincerely yours,

Carroll South, Executive Director
Montana Board Of Investments